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AN ANALYSIS OF INSIDER TRADING LAW AND CASES IN THE MALAYSIAN SECURITIES MARKETS

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ABSTRACT

The securities markets play a very significant role in the development of economic and business activities in the global environment. In Malaysia, it is evidenced through the achievement of the Malaysian capital market with fund raising approved by the Securities Commission Malaysia (SC) reaching RM118.93 billion at the end of 2011, compared to RM77.02 billion in 2010. In order to maintain investors confidence in the securities markets, there is a need for securities markets activities to be regulated and its must be rigorously enforced. Insider trading in securities markets is classified as one of the prohibited conduct under the Capital Markets and Services Act 2007 (CMSA 2007) of Malaysia. It is regulated under Sub Division 2, section 183 until 201 of the CMSA 2007. This paper critically analyzed the provisions of law and regulations and highlighted insider trading cases in Malaysia from the year 2010-2012. The source of legal data is from primary and secondary sources. The findings of research shows that the insider trading laws and enforcement are sufficient but there are a few improvements to be executed by the Securities Commission, self-regulatory bodies and corporations.

Keywords: Insider trading, securities markets, law, securities crimes, inside information

1. Introduction

The Malaysian capital market continued to grow with fund raising approved by the Securities Commission Malaysia (SC) reaching RM118.93 billion at the end of 2011, compared to RM77.02 billion in 2010 (Securities Commission, 2012). This marked increase reflects strong confidence in the fund raising environment and sukuk approvals which had more than doubled to RM78.9 billion from RM38.3 billion the year before. The approvals included the world's largest corporate sukuk programme of RM23.3 billion by Projek Lebuhraya Usahasama Berhad, under which issuance commenced in January 2012. Malaysia remains at the forefront of the sukuk market, accounting for 73% of the total sukuk issued globally (Securities Commission, 2012). Further, taking into consideration changes in the global and domestic financial landscape, significant amendments to the *Securities Commission Act 1993* (SCA) and

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the *Capital Markets and Services Act 2007* (CMSA) came into force on 3 October 2011 to strengthen the regulatory framework of the capital market in line with global standards and pursuant to the strategies outlined in the CMP2. The amendments focused on internationalising and enhancing the competitiveness of the Malaysian capital market with changes to expand the mandate of the SC to promote market stability, as well as to ensure effective regulatory oversight over trustees and custodians. The licensing provisions in the CMSA were also amended to promote ease of doing of business and facilitate a more cost effective regulatory regime without compromising investor protection. The regulatory reforms also strengthened the SC's regulation of OTC derivatives with a trade repository to be introduced (Securities Commission, 2012)

Therefore, in order to maintain investors confidence in the securities markets, there is a need for securities markets activities to be regulated and its must be rigorously enforced. In Malaysia, the Capital Markets and Services Act 2007 (CMSA 2007) is the main statute which regulates all prohibited conducts in the securities and derivatives markets. Other statutes which regulate the capital markets are Securities Commission Act 1990, Companies Act 1965 and a few others. There are many types of prohibited conduct in securities markets i.e. false trading, market rigging, stock market manipulations, false and misleading statements, fraudulent inducing persons to deal in securities, use of manipulative and deceptive devices, dissemination of information about illegal transactions and insider trading (section 175 to section 198, CMSA 2007). Whether these provisions is well drafted and managed to protect investor's interest or not, will be discussed later in the paper with attention be given to the offence of insider trading. Next, whether the enforcement strategies by the Securities Commission and Bursa Malaysia (as a self-regulatory organization) produced a significant impact in reducing numbers of insider trading cases in Malaysia, is another aspect that will be analyzed by the researcher.

As announced by the government of Malaysia, the main objective of the implementation of insider trading and other prohibited conducts regulation in Malaysia is to maintain the integrity and as protection to investor's interests in the securities markets. Similarly, in the case of Singapore, after the notorious *Baring's* scandal, the Singaporean government reviewed and made significant amendments to their securities regulation including insider trading law (2007, Howard Chua-Eoan). In the United States, a finding of research by Seyhun (1992) shows that corporate insiders earned an average of 5.1% abnormal profits over a one year holding period between the years of 1980 - 1984, increasing further to 7% after 1984.

Therefore, the paper will critically analyzed the provisions of law and regulations and highlighted insider trading cases in Malaysia from the year 2010-2012.

2. Literature Review

Insider trading has been practiced in the securities market industry because of the use of special knowledge that can lead to enormous profits being made and in such a situation the questions of fairness and equal access to information will be regarded as meaningless to a few persons who have access to inside information. (Asmah Laili, 1999). Inside information is a valuable privilege. According to Haft (1982), it is doubtful whether the board of directors and chief executive officer would voluntarily

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eliminate their own potentially immense profits nor would the employees of a corporation. Therefore, the existence and enforcement of insider trading law can assist to curb unethical practices such as insider trading amongst participants of the industry.

The purpose of publication of legislation or rules is to inform and to act a preliminary warning to market participants and the public as a whole, which actions are wrong and which are permitted. If there are no laws or rules regarding insider trading, further distortions in company share prices caused by the manipulation of disclosures by insiders may obstruct not only the market's allocative efficiency, but also its liquidity and may increase the cost to companies wishing to raise capital (Knight, 1935).

In Malaysia, the SC's steady focus on enforcement by criminal actions in 2011 achieved the highest number of custodial sentences in the history of the SC's enforcement efforts. The year of 2011 was a benchmark year in terms of custodial sentences handed down by the courts where 13 persons received custodial sentences and the courts imposed fines totaling in excess of RM13.7 million. This including a landmark decision for securities cases, the Court of Appeal upheld a six-month jail term imposed by the High Court on two former directors of MEMS Technology Bhd for authorising a misleading statement to the stock exchange in the company's financial statements. In a case involving criminal breach of trust, a former director of Multi-code Electronics Industries was sentenced to 12 years imprisonment while another director received a jail sentence of six years. The Kuala Lumpur Sessions Court also sentenced a director of FX Consultant Sdn Bhd and FX Capital Consultant Sdn. Bhd. to five years' imprisonment and a fine of RM5 million for operating a *ponzi* scheme and taking part in money laundering, marking one of the heaviest punishments against a capital market offender.

3. Research Methodology

This is a qualitative legal research paper. The source of legal data is from primary and secondary sources. The researcher analyses provisions of statutes, court cases, articles, books and tertiary data which are relevant to the research paper. Insider trading cases discussed in the paper covered only for the period of three years from 2010 to 2012. These are all recent cases which been prosecuted by the Securities Commission and brought to the court of justice.

4. Findings of Research

This part will discuss and analyse provisions of law of insider trading under the CMSA 2007 and highlighted cases of insider trading from 2010 to 2012.

a. Analysis of insider trading provisions

Definition of Insider Trading

Insider trading is a situation where a person takes advantage of information which is not publicly available by dealing on the basis of it in securities where the prices are materially affected. According to section 188 of the CMSA 2007, insider trading happens when a person possesses information that is not generally available which on becoming generally available a reasonable person would expect it to have a material effect on the price or the value of securities and knows or ought reasonably to know. According to the provision, an insider cannot (a) acquire or dispose or enter into an agreement or procure directly or indirectly an acquisition or disposal of or the entering into an agreement; or (b) procure, directly or indirectly, an acquisition or disposal of or enter into an agreement for the acquisition (section 188 (2), CMSA 2007).

Besides defining the crime of insider trading, the CMSA 2007 also states the scope of information, information generally available and the meaning of material effect on price or value of securities. By analyzing the definition of information in section 183 of the CMSA 2007, obviously the researcher is of the opinion that it is widely defined. It does not help much to investors nor participants nor players of the industry to identify and understand the limit in abstaining themselves from doing the unethical practices. However, with the existence of the Listing Requirements of Public Listed Companies (PLCs), specific example has been highlighted as guidelines to the PLCs. But, we have to refer to two different sources to understand it. General definition in a statute provides advantages and disadvantages. The advantages is that to the court, it can play an important role to define and develop the law itself and also give advantages to the legal practitioner to argue and state their legal opinion on the matter. These will make the law alive and not static. However, for participants of the industry or laymen perspectives, if the law is too vague, then it will be difficult to discipline oneself or organization to abide with the rule or regulation because it is open for different interpretation.

Research finding by Asmah Laili and Faridahwati (2010) showed that ambiguity of the law and regulations is one of the factors for non compliance of the Disclosure Based Regulation in the capital markets of Malaysia (mean value = 4.029). Therefore, it is very important to disseminate quality and clear information to investors and players of the industry. Material information about law and regulations is utmost important to society because they are the one who are the key player in any businesses or social activities. The writer is of opinion that the CMSA 2007 particularly section 183 should elaborate more about the scope of information by importing some material examples as in the Listing Requirements of PLCs.

Even though in the CMSA 2007 did not mentioned about the secondary insider or tippees directly but elaboration in section 188(2) and (3) showed that this category of insider also is within the scope of insider as mentioned in sub section (1) of the provision.

In the CMSA 2007 also includes exceptions of certain dealings which are not considered as the act of insider trading. These are (1) secrecy arrangements by corporation and partnerships; (2) underwriting and sub underwriting; (3) transactions under scheme of arrangements; (4) corporation with knowledge of its intention; (5) knowledge of individual’s own intentions or activities; (6) unsolicited transaction; (7)

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redemption of units of unit trust scheme under buy-back covenant; and (8) parity of information defence (sections 190 – 198 of the CMSA 2007). In these cases, in a prosecution of an offence of insider trading, it is not necessary for the prosecution to prove the non-existence of facts or circumstances which if they existed, preclude the act constituting an insider trading act. The list of defences of insider trading in the CMSA 2007 helps investors and players of the capital markets industry to be aware of the boundary of insider trading activities. Therefore, this showed the example of transparency of regulations in the Malaysian securities industry.

c. Analysis of Criminal Sanctions and Civil Actions And Regulatory Settlements

Under the CMSA 2007, there are several ways on how the SC has been given powers to protect victims and combating criminals of insider trading offence. Firstly, by enforcing criminal sanctions which is stipulated in section 188(4) of the CMSA 2007 where it says that any person contravenes section 188(2), commits an offence and will be punished on conviction to imprisonment for a term not exceeding ten years and to a fine of not less than one million ringgit.

Secondly, by civil actions and regulatory settlements where according to section 201(5) and (6) of the CMSA 2007, the SC may if it considers that it is in the public interest to do so, by civil action against the insider or any other person involved in the contravention recover an amount of equal to three times the amount being the difference between the price at which the securities were acquired or disposed. Further, the SC also can claim civil penalty in such amount as the court considers appropriate having regard to the seriousness of the contravention, being an amount not more than one million ringgit.

The following discussion is referring to cases regarding civil actions and regulatory settlements of insider trading cases in Malaysia. The recent case of insider trading is on 3 February 2012, the SC entered into a settlement with Lim Chin Chin in the sum of RM232,320 when she agreed without admission or denial of liability to settle a claim that the SC was proposing to institute against her for insider trading in the shares of Sin Chew Media Corporation Berhad ('Sin Chew') between 29 January 2007 and 30 January 2007, contrary to Section 89E(3)(a) of the Securities Industry Act 1983 (now known as the Capital Markets and Services Act 2007). The settlement was reached following a letter of demand sent by the SC pursuant to its civil enforcement powers under the securities laws, where the sum Lim Chin Chin was required to disgorge was equivalent to three times the gains made by Ong Sew Teng and Chong Hiong Lim in connection with their trades in Sin Chew shares.

In the case of Sreesanthan A/L Eliathamby, he was charged 20 July 2012 with seven counts of insider trading under section 188(2)(a) of the Capital Markets and Services Act (CMSA) and section 89E(2)(a) of the Securities Industry Act (SIA). He was alleged to have traded in the shares of four public listed companies while in possession of inside information relating to various corporate exercises, details of which are stated below:

- Sime Darby Berhad while in possession of the proposed acquisition by Synergy Drive of companies within the Sime Darby, Guthrie and Golden Hope groups.

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- Maxis Communication Bhd while in possession of Maxis' privatisation.
- UEM World Berhad while in possession of the corporate restructuring exercise of the UEM group.

VADS Berhad while in possession of VADS's proposed privatisation. This case is still pending in court.

Compared to 2011, in the 2012 the number of cases of insider trading were reduced significantly.

Looking back in the year of 2011, there were a few cases where the SC successfully entered into a settlement. The first case is Rameli's case where on 16 November 2011, the SC entered into a settlement with Rameli bin Musa in the sum of RM36,050 when he agreed without admission or denial of liability, to settle a claim that the SC was proposing to institute against him for insider trading in the shares of Crest Petroleum Berhad (Crest) between 15 January 2003 and 17 January 2003, contrary to section 89E of the Securities Industry Act 1983 (SIA). The settlement was reached following letters of demand sent by the SC pursuant to its civil enforcement powers under the securities laws, where the sum Rameli bin Musa was required to disgorge was equivalent to three times the gains he made from his trades in Crest shares. In accordance with the provisions of section 90A(7) of the SIA, the amount recovered from Rameli bin Musa will be used first to reimburse the SC for all costs of investigations and proceedings. The remaining amount will be used to compensate the sellers who sold their shares to him before the information became generally available.

Further, On 13 October 2011, the SC entered into a settlement with Chong Mei Ngor in the sum of RM88,110 when she agreed without admission or denial of liability, to settle a claim that the SC was proposing to institute against her for insider trading in the shares of Sin Chew Media Corporation Berhad (Sin Chew) between 25 January 2007 and 30 January 2007, contrary to section 89E of the Securities Industry Act 1983 (SIA). The settlement was reached following letters of demand sent by the SC pursuant to its civil enforcement powers under the securities laws, where the sum she was required to disgorge was equivalent to three times the gains she made from her trades in Sin Chew shares. In accordance with the provisions of section 90A(7) of the SIA, the amount recovered from Chong Mei Ngor will be used first to reimburse the SC for all costs of investigations and proceedings. The remaining amount will be used to compensate the sellers who sold their shares to her before the information became generally available.

In other case, on 3 October 2011, the SC entered into a settlement with Foong Choong Heng in the sum of RM281,361 when he agreed without admission or denial of liability, to settle a claim that the SC was proposing to institute against him for insider trading in the shares of Crest Petroleum Berhad (Crest) between 14 January 2003 and 21 January 2003, contrary to section 89E of the Securities Industry Act 1983 (SIA). The settlement was reached following letters of demand sent by the SC pursuant to its civil enforcement powers under the securities laws, where the sum he was required to disgorge was equivalent to three times the gains he made from his trades in Crest shares. In accordance with the provisions of section 90A(7) of the SIA, the amount recovered from Foong Choong Heng will be used first

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to reimburse the SC for all costs of investigations and proceedings. The remaining amount will be used to compensate the sellers who sold their shares to him before the information became generally available.

Again, on 3 October 2011, the SC entered into a settlement with Ong Sew Teng in the sum of RM71,280 when she agreed without admission or denial of liability, to settle a claim that the SC was proposing to institute against her for insider trading in the shares of Sin Chew Media Corporation Berhad (Sin Chew) between 24 January 2007 and 30 January 2007, contrary to section 89E of the Securities Industry Act 1983 (SIA). The settlement was reached following letters of demand sent by the SC pursuant to its civil enforcement powers under the securities laws, where the sum she was required to disgorge was equivalent to three times the gains she made from her trades in Sin Chew shares. In accordance with the provisions of section 90A(7) of the SIA, the amount recovered from Ong Sew Teng will be used first to reimburse the SC for all costs of investigations and proceedings. The remaining amount will be used to compensate the sellers who sold their shares to her before the information became generally available.

Further, also on 3 October 2011, the SC entered into a settlement with Chong Hiong Lim in the sum of RM161,040 when he agreed without admission or denial of liability, to settle a claim that the SC was proposing to institute against him for insider trading in the shares of Sin Chew Media Corporation Berhad (Sin Chew) between 25 January 2007 and 30 January 2007, contrary to section 89E of the Securities Industry Act 1983 (SIA). The settlement was reached following letters of demand sent by the SC pursuant to its civil enforcement powers under the securities laws, where the sum he was required to disgorge was equivalent to three times the gains he made from his trades in Sin Chew shares. In accordance with the provisions of section 90A(7) of the SIA, the amount recovered from Chong Hiong Lim will be used first to reimburse the SC for all costs of investigations and proceedings. The remaining amount will be used to compensate the sellers who sold their shares to him before the information became generally available.

Similarly, the SC entered into a settlement on 3 October 2011, with Soon Khiat Voon in the sum of RM33,750 when he agreed without admission or denial of liability, to settle a claim that the SC was proposing to institute against him for insider trading in the shares of Sin Chew Media Corporation Berhad (Sin Chew) between 25 January 2007 and 30 January 2007, contrary to section 89E of the Securities Industry Act 1983 (SIA). The settlement was reached following letters of demand sent by the SC pursuant to its civil enforcement powers under the securities laws, where the sum he was required to disgorge was equivalent to three times the gains he made from his trades in Sin Chew shares. In accordance with the provisions of section 90A(7) of the SIA, the amount recovered from Soon Khiat Voon will be used first to reimburse the SC for all costs of investigations and proceedings. The remaining amount will be used to compensate the sellers who sold their shares to him before the information became generally available.

On 28 September 2011, the SC entered into a settlement with Parmjit Singh a/l Meva Singh and Sushil Kaur a/p Dulla Singh in the sum of RM83,513 when they agreed without admission or denial of liability,

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to settle a claim that the SC was proposing to institute against them for insider trading in the shares of Crest Petroleum Berhad (Crest) between 14 January 2003 and 16 January 2003, contrary to section 89E of the Securities Industry Act 1983 (SIA). The settlement was reached following letters of demand sent by the SC pursuant to its civil enforcement powers under the securities laws, where the sums both of them were required to disgorge was equivalent to three times the gains they made from their trades in Crest shares. In accordance with the provisions of section 90A(7) of the SIA, the amount recovered from them will be used first to reimburse the SC for all costs of investigations and proceedings. The remaining amount will be used to compensate the sellers who sold their shares to them before the information became generally available.

Whereas on 18 September 2011, the SC entered into a settlement with Lee Kwong Joo in the sum of RM18,000 when he agreed without admission or denial of liability, to settle a claim that the SC was proposing to institute against him for insider trading in the shares of Sin Chew Media Corporation Berhad (Sin Chew) between 25 January 2007 and 30 January 2007, contrary to section 89E of the Securities Industry Act 1983 (SIA). The settlement was reached following letters of demand sent by the SC pursuant to its civil enforcement powers under the securities laws, where the sum he was required to disgorge was equivalent to three times the gains he made from his trades in Sin Chew shares. In accordance with the provisions of section 90A(7) of the SIA, the amount recovered from Lee Kwong Joo will be used first to reimburse the SC for all costs of investigations and proceedings. The remaining amount will be used to compensate the sellers who sold their shares to him before the information became generally available.

On 29 March 2011 the SC entered into a settlement with Mr Heah Sieu Lay in the sum of RM77,576 when he agreed, without admission of liability to make the payment. This sum constituted a disgorgement of twice the profits arising from alleged irregularities in his trading of Nexnews Berhad shares between 4 May 2007 and 10 May 2007. This settlement followed the SC's proposed proceedings under section 89E and 90(1) of the Securities Industry Act 1983.

On 29 March 2011 the SC entered into a settlement with Mr Tan Kong Han in the sum of RM24,760 when he agreed, without admission of liability to make the payment. This sum constituted a disgorgement of twice the profits arising from alleged irregularities in his trading of Nexnews Berhad shares between 3 May 2007 and 17 August 2007. This settlement followed the SC's proposed proceedings under section 89E and 90(1) of the Securities Industry Act 1983.

On 22 March 2011 the SC entered into a settlement with Kanesan a/l Veluppillai in the sum of RM98,247 when he agreed, without admission of liability to make the payment. This sum constituted a disgorgement of three times the profits arising from alleged irregularities in his trading of Nexnews Berhad shares between 3 May 2007 and 10 May 2007. This settlement followed the SC's proposed proceedings under section 89E and 90(1) of the Securities Industry Act 1983.

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From the above cases, in the year of 2011, it can be concluded that the range of settlement (in Ringgit Malaysia) is from RM18,000.00 to the maximum of RM282,000.00. There were differences in value for each of the case because of the decision was made based on merit of case. However, from the perspective of criminal sanction, whether this settlement is at par with the seriousness of the offence of insider trading is still questionable. This is because looking at the criminal sanction the minimum penalty is not less than one million (Ringgit Malaysia) and imprisonment for a term not exceeding ten years. Even if we refer to section 201(5)(b) gives a power to the SC to claim civil penalty in a larger amount as the court considers appropriate having regard to the seriousness of the contravention being an amount not more than one million but this was not practiced.

In the year of 2010 there was one case reported by the SC that is the case of Kenmark Industrial (M) Sdn Bhd (Kenmark) and Ishak Ismail. Ishak Ismail as the majority shareholder of Kenmark was suspected of making false or misleading statements in relation to the condition of Kenmark which had the effect of raising the market price of Kenmark shares. Datuk Ishak was also suspected of trading on Kenmark's shares based on the inside information. This case is pending in court.

From the finding showed that most of insider trading cases were successfully settled in a way of civil sanctions and regulatory settlements. This is referred to insider trading cases in the year of 2011 as highlighted above. In the case of *Smith New Court Securities Ltd v Scrimgeour Vickers (Asset Management) Ltd. [1996] 4 All ER 769* highlights the importance of the compensatory damages in combating the effects of fraud. The House of Lords acknowledge that the principal of the law of tort/delict is to compensate the victims of wrongdoings for loss suffered through the commission of a wrong, but they indicated that more stringent liability may be imposed on an intentional wrongdoer, as opposed to morally reprehensible defendant. As Lord Steyn said:

"In the battle against fraud, civil remedies can play a useful and beneficial role. Secondly, as between the fraudster and the innocent party, moral considerations militate in favour of requiring the fraudster to bear the risk of misfortunes directly caused by his fraud."

Administrative actions by the SC and Bursa Malaysia against licensed holder of securities and derivatives markets are also other alternative sanctions. According to Lee (1993), the advantages includes speed of action where impending breaches must be stopped, regulatory authority is both the prosecutor and judge where it allows for consistency in the interpretation of provisions and the implementation of the policy and lastly the regulatory can impose appropriate punishments such as suspension of profits, money penalties, all in the same proceedings.

5. Conclusion and Future Recommendation

As discussed above, there are negative effects of insider trading to the markets, companies and lastly to investors' confidence. The author is of the view that insider trading would be very damaging if not

curbed by the relevant authority because it will cause a sharp decline of participation in the securities market itself. The loss of confidence occurs when the investor perceive that there were other parties profiting through dealing with inside information. Obviously, investors would not want to take the risk when they know that they are in a losing position. It is more prudent to invest in another sort of investment which is relatively secure.

Therefore, adopting different strategies in combating insider trading by several countries such as Malaysia, Hong Kong, United States, United Kingdom, Australia and others is very sensible. Different regulatory mechanism to control and prevent insider trading activities must be performed. These include market entry controls, conduct of business requirements, anti-fraud provisions, monitoring, enforcement and disciplinary measures by the regulators.

Further, leaders and management should promote and adhere to sound values and standards. Within every organization, most individuals will follow the crowd. Therefore, the top management must set out realistic policies and procedure to prevent insider trading activities occurred among themselves or their staffs. All public companies in Malaysia should adopt transparency in marketing their products and disclosure of material information should be the priority measure for companies so as to create transparent environment and an informed market.

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